

GENERALIZED SYSTEM OF PREFERENCES TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

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GENERALIZED SYSTEM OF PREFERENCES TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The objective of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for Generalized System of Preferences (GSP) and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and the terms in this document are based on *Assessing Internal Controls in Performance Audits*, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountants *Statement on Auditing Standards No. 78*.

PART 2 GENERALIZED SYSTEM OF PREFERENCES GUIDANCE

Title V of the Trade Act of 1974 (19 U.S.C. 2461-2465), as amended, which authorized the President to establish GSP to provide duty-free treatment for eligible articles imported directly from designated beneficiary developing countries (BDCs).

The eligible BDCs are listed in General Note 4 of the Harmonized Tariff Schedule of the United States (HTSUS). General Notes 4(a) and 4(b) provide the list of BDCs, the combinations of BDCs treated as one country and the least developed BDCs eligible for GSP treatment.

General Note 4(c) provides general exceptions by merchandise description to GSP, and 4(d) provides specific exceptions by specific BDC country and HTSUS number not eligible for GSP treatment.

Title 19 CFR 10.171 through 10.178 states the regulations for GSP.

GSP allows duty-free treatment for goods meeting certain eligibility requirements on entry into the United States. To qualify for GSP, goods must meet the following requirements:

- The imported goods must come to the United States directly from the GSP-eligible country; the direct shipment requirements are in 19 CFR 10.174 and 10.175.
- The imported goods must be wholly the growth, product, or manufacture of the BDC, or a new or different article of commerce that has been grown, produced, or manufactured in a BDC, as stated in 19 CFR 10.176 (a).
- The imported goods must meet the value content requirements of 19 CFR 10.176 through 10.178. GSP merchandise that is not wholly the growth, product, or manufacture of a BDC may be accorded duty-free treatment only if the direct costs of processing performed in the BDC plus the cost or value of materials produced in the BDC is not less than 35 percent of the appraised value.

Information can be requested from the producer using the table provided in 19 CFR 10.173(a)(1). The information requested shall be submitted within 60 days of the date of the request or such additional period as may be allowed for good cause shown.

GSP eligibility is reported using the letter A (the letter Q is used where GSP has expired with the possibility that privileges may be reinstated) in the Special Program Indicator column of the Automated Commercial System (ACS) database. Where an imported good is eligible for GSP, the letter A is also listed in special rates of duty part of Column 1 of the HTSUS. Where the HTSUS indicates an A+ in the Column 1 special rates of duty, the duty-free rate applies only to the least developed BDCs listed in General Note 4(b). Where the special rates of duty part of Column 1 of the HTSUS indicates an A* notation for a specific HTS number, certain BDCs listed in General Note 4(d) are not eligible for GSP for the designated HTS number.

Additional guidance is found in the publication “A Guide for Supporting Generalized System of Preferences (GSP) Claims” (FA Kit Exhibit 4F).

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem in GSP.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring GSP for Customs purposes. Examples:
 - ✓ Company does not monitor or interact with the broker on GSP issues.
 - ✓ Company relies on one employee to handle GSP issues, and there are poor or no management checks or balances over this employee.
- Company Customs staff lacks knowledge of GSP eligibility issues.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate or respond to Customs.
- Company has high turnover of people in key positions.
- Significant variance exists between the importer's data and Customs data.
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with GSP (e.g., GSP eligibility issues or reporting incorrect country of origin).
- One company representative dominates multiple phases of the GSP process without monitoring or management oversight.
- High compliance measurement error rates occur for HTSUS numbers that the company frequently uses regarding GSP.
- The company imports from a specific provider or under an HTSUS number or country of origin that have been identified by Customs because of known or suspected GSP problems.
- The company imports indicate a large number of GSP Manufacturer Identification (MIDs).
- The company imports a large quantity of GSP articles over many HTSUS numbers.
- The company does not monitor of the GSP classification or records process.
- The company imports of GSP increase significantly from a prior period.
- The importer and the GSP producer are related.
- GSP imports have not been previously audited or reviewed by Customs.
- Specific issues are identified in the profile.
- Company does not request, maintain, or review documents supporting the qualification of GSP (e.g., value content qualification).
- The company Imports some GSP articles that may be considered sets, mixtures, or composites (see T.D. 91-7 and HQ ruling 559010, dated 3/14/96) that could preclude GSP eligibility.
- The company imports some GSP articles which, in addition to a value content requirement, may require a “double substantial transformation” (see CSD 85-25, which explains 19 CFR 10.177(a)(2)).
- Value content qualification is marginal, just meeting the 35 percent requirement, increasing the importance of accurate cost computations.
- Direct materials alone are not adequate to meet the 35 percent value content requirement, making accurate direct processing costs particularly important.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over GSP:
 - ✓ Are in writing,
 - ✓ Include procedures for monitoring and feedback, and
 - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the Import Department, including GSP. That manager has knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign GSP duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about GSP matters.
- Company conducts and documents periodic reviews of GSP, and uses the results to make corrections past and present to entries and changes to its import operations as appropriate.
- Purchasing, Engineering, other departments and suppliers provide sufficient descriptions of merchandise to permit a determination of GSP eligibility.
- Internal control includes a verification process to determine that the imported merchandise qualifies for GSP.
- Importer has procedures to obtain any required or necessary documentation to support the claim (e.g., a penalty provision on suppliers if GSP information is not provided to Customs on demand).
- Importer maintains a GSP database or listing of imported merchandise that would readily identify GSP transactions.
- The importer (or the importer's agent) visits the plant in the GSP country where the products are produced.
- The importer performs an annual review of changes to GSP.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures for ensuring proper GSP eligibility.
- Company's response to the questionnaire.
- Interviews with company staff concerning general internal control and internal control specific to GSP.
- Company's documentation that supports monitoring and verification of established and/or written internal control for GSP, including:
 - ✓ GSP declaration signed by the person responsible for certifying that all information on the documentation is accurate and complete.
 - ✓ If available from the importer, the GSP costing sheet.
 - ✓ Binding rulings concerning GSP.
 - ✓ Invoices, specification sheets, or other documents providing detailed descriptions of GSP merchandise.
 - ✓ List containing GSP part numbers, descriptions, quantities imported, and unit costs.
 - ✓ Bills of lading or other evidence of direct transport to the United States.
 - ✓ Producer's written attestation that goods are wholly the growth or product of a BDC.
 - ✓ Records from the GSP producer supporting the company's verification for goods not wholly the growth or product of a BDC, such as GSP cost allocation worksheets, bills of materials, product specification sheets, engineering drawings, work-in-process documents, material inventory records, purchase history reports, and/or material supplier lists.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgment should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and
2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

Examples of Preliminary Assessment of Risk

Example A: Low Risk

The import specialist, the account manager, and the profile did not identify any concerns with this importer's GSP program. The importer stated that all GSP came from one supplier. The import was wholly the growth of the country of export and the country was one of three major exporting countries of the commodity in the world. Because there were no PAS team concerns, the assessment of risk was considered low.

Example B: High Risk

The import specialist, the account manager, and the profile identified specific concerns with this importer's GSP program. GSP merchandise was frequently misclassified and was sometimes not eligible for GSP when it was correctly classified. The company was the 10th largest importer of GSP. For the year of audit, the importer stated that all GSP came from 10 manufacturers. Because non-GSP imports could be incorrectly listed as GSP, the assessment of risk was considered high.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.
- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:
 - Control Environment
 - Risk Assessment
 - Control Activities
 - Information and Communication
 - Monitoring
2. Review relevant Customs and company documents to identify and understand relevant internal control over GSP. (Examples of documents and information to review are listed above.)
3. Determine whether the company has established and follows procedures. Review:
 - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
 - Documentary evidence (such as a log) of communication with the broker and company departments on GSP issues, including company testing of broker operations and verification that the broker followed company instructions.
 - Company-specific GSP rulings requested. Determine if they are followed.
 - Documentary evidence of intercompany communications, to ensure that correct information is provided to Customs.
 - Training records and materials relating to GSP used to educate staff on Customs matters.
4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for Generalized system of Preferences (GSP).

Note: The internal control assessment should include steps to:

- Identify and understand internal control
- Determine what is already known about control effectiveness
- Assess the adequacy of internal control design
- Determine whether controls are implemented and effective
- Determine whether transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it

probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the total GSP level that will be reported on. For example, the company may import from several foreign companies, but testing may be necessary only for certain companies or only for certain imports that have been identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review/ Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits*.
Column titled "Testing Limit" reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over GSP.

1. Complete the WEIC for GSP to determine whether risk is acceptable or unacceptable and document why. Put results of GSP testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.
2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT:

Do not proceed to ACT if:

- Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
- The result of review indicated that the error was due to an isolated incident.
- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

Proceed to ACT if:

- The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations might be encountered under PAS are for clarification purposes only.

Example A: Situation in which the team would not proceed to ACT (Revenue)

The importer has internal control for GSP. The internal control includes contract provisions in which the exporter agrees to provide documentary support for GSP eligibility to Customs on demand; reviews of foreign facilities to verify foreign production in the BDC; and maintenance of documentary information to support importer reviews and testing of GSP eligibility. In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of GSP eligibility data, including cost data, supported the eligibility of products from all GSP manufacturers except Happy Link. The team concluded that internal control was effective for shipments of all manufacturers except Happy Link. The breakdown in internal control was systemic. The importer had not included the GSP contract provisions in the contract negotiated with Happy Link. When Customs, as part of the limited testing for GSP, required that Happy Link provide support for GSP eligibility for the items sampled, the manufacturer refused. The entries were not liquidated. The importer agreed to quantify and pay the lost revenue on the Happy Link imports and change its internal control procedures. All future contracts will be amended to include GSP requirements *before* merchandise is declared as eligible for GSP. Since there were no other revenue issue and correction was made to avoid future problems, the team does not proceed to ACT for revenue.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same as example A above, except that the importer agrees to amend the contract with Happy Link to include the GSP provisions immediately, and Happy Link sends the requested country of origin information to Customs. Since the importer agreed to correct internal control deficiencies and Happy Link's merchandise was determined to be GSP eligible, there is no reason to proceed to ACT for compliance.

Example C: Situation in which the team would proceed to ACT (Revenue)

Same as example B above, except that preliminary analysis indicates that for some imports, Happy Link provided the data required by the controls; thus, some of the imports from Happy Link may qualify for GSP (and others do not). Imports from Happy Link included a large volume

of low-value items. The importer is unable to quantify the GSP-eligible value in the Happy Link account. The PAS team proceeds to ACT to use statistical sampling to project revenue loss.

Example D: Situation in which the team would proceed to ACT (Compliance)

The same as example C above, except that preliminary analysis indicates that some of the imports from Happy Link may qualify for GSP. The importer agrees to pay duty on imports for the one Happy Link contract found during the PAS as outside GSP internal control. The importer does not want to change its current internal control and believes that it meets an acceptable level of compliance for GSP (i.e., importer indicates that the internal control breakdown was an isolated event). Since the importer will not change its internal control and the level of compliance is unknown, the PAS team proceeds to ACT to determine whether the importer meets the acceptable level of compliance for GSP.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - Generalized System of Preferences (GSP)

PURPOSE: To determine whether GSP risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: <ul style="list-style-type: none"> • Interview and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 – Sample Sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4-Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 –Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 - Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Does the company have formally documented internal control to assure that GSP is correctly declared?					
2.	Does management approve written policies and procedures?					
3.	Does the company review and update written policies?					
4.	Is internal control over GSP periodically tested and results documented? (This should include post-entry reviews to verify correctness of GSP.)					
5.	When the company identified weaknesses during internal control testing of GSP entries, did the company correct internal control procedures and related entries when appropriate?					
6.	Do written internal control procedures assign responsibility for GSP to a position rather than an individual?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does one individual have authority to ensure that internal control procedures for GSP are established and followed by all company departments?					
8.	Do personnel responsible for ensuring GSP is correct have adequate knowledge and training in GSP?					
9.	Does the company have adequate interdepartmental communication about GSP?					
10.	Does the company have procedures to request Customs assistance concerning GSP when needed and is advice followed when given (e.g., requesting binding rulings)?					
11.	Does the company identify, analyze, and manage risks related to GSP?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
12.	Has the company identified any risks related to GSP and implemented control mechanisms?					
13.	Does the company have policies and procedures in place to ensure that new merchandise is GSP eligible? Specifically:					
	a. Does the company have a verification process to determine that imported merchandise qualifies for GSP?					
	b. Does the importer have procedures to obtain required documentation to support the claim?					
	c. Does the importer (or agent) visit the plant in the BDC where the products are produced?					
	d. Does the company have procedures to ensure that GSP eligible goods were directly imported from a BDC?					
	e. Does the company ensure that only the costs identified in 19 CFR 10.177 and 10.178 are included in the 35 percent calculations?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	Does the company conduct and document periodic monitoring of GSP claims?					
	a. Are documents supporting eligibility reviewed for correctness?					
	b. Are classifications reviewed to determine correctness and eligibility?					
	c. Are material and processing costs re-evaluated to determine that they still meet the 35 percent cost requirement?					
	d. Are results of reviews used to make corrections to past and future entries?					
	e. Are results of reviews used to correct internal control system weakness?					
15.	Does the company provide adequate broker oversight of GSP issues?					
	a. Is the broker required to obtain company concurrence prior to making changes to GSP claims/entries?					
	b. Are GSP entries reviewed to determine that broker used correct GSP-eligible classification?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	c. Are GSP entries reviewed to determine that the merchandise was GSP eligible?					
16.	List company-specific procedures below (if applicable).					

Section 2 - Preliminary Internal Control Assessment

Use Information obtained in Section 1 above to make a preliminary assessment of internal control as strong, adequate weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

*If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in Section 3.3 of TIPS to determine the extensiveness of audit test to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
IC is effective to provide reasonable assurance to preclude significant risk.	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable?		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.